

PART 329 – INTEREST ON DEPOSITS

OVERVIEW

Part 329 of FDIC Rules and Regulations prohibits the payment of interest on *demand deposits* and limits eligibility for *Negotiable Order of Withdrawal (NOW)* accounts.

Examination Objective(s)

The objectives of the examination are to:

Identify the types of deposit accounts the financial institution offers

Determine that the financial institution is not allowing ineligible entities to maintain NOW accounts

Determine that interest is not being paid on demand deposits

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DEFINITION(S)

Cash Management Arrangements

Cash management services provided by financial institutions sometimes include offering sweep accounts and repurchase agreements. Regulatory compliance for these activities is generally reviewed during safety and soundness examinations. However, examiners should be aware that Section 329.2 concerning the prohibition of paying interest on demand deposits could be violated based on the definitions of Money Market Deposit Accounts (MMDA) and savings accounts for excessive transactions.

DEFINITION(S)
(cont'd)

**Money Market
Deposit Account
(MMDA)**

An MMDA is a savings deposit that permits, under the terms of the deposit contract or by practice of the financial institution, the depositor to make no more than six transfers and withdrawals per calendar month or statement cycle of at least four weeks to another account of the depositor or to a third party.

No more than three of the six transfers can be made by check, draft, debit card, or similar order to a third party. The following transfers **are not included** in the six transfer limitation:

Transfers to the financial institution for the purpose of repaying loans and associated expenses (as originator or servicer).

NOTE: This exemption "does not apply to transfers to the financial institution that are made for the purpose of repaying loans that are made by the financial institution to the depositor's demand deposit account for the purposes of covering overdrafts." (Section 329.1(b)(3))

Transfers to another account of the depositor made by mail, messenger, automated teller machine (ATM), or in person

Withdrawals made by mail, messenger, telephone (via check mailed to the depositor), ATM, or in person

Refer to Section 204.2(d) of Regulation D and the Interpretative Rule found in Section 329.101 for more guidance on MMDAs.

NOW Account

NOW Accounts are deposit accounts which consist solely of funds in which the entire beneficial interest is held by:

One or more individuals, including sole-proprietorships

A not-for-profit organization operated primarily for religious, philanthropic, charitable, educational, political, or other similar purpose

Officers, employees, or agents of public entities (public funds)

Funds held in a fiduciary capacity (bank trust department, individual fiduciary, or trustee in bankruptcy), provided that all beneficiaries are natural persons

DEFINITION(S)
(cont'd)

The following types of entities **are not** eligible to maintain NOW accounts:

NOW Account
(cont'd)

Corporations

For-profit partnerships, including a husband and wife partnership

Individuals who have incorporated, such as Professional Associations (PA)

Trust accounts where the beneficial interest is held by two or more unrelated parties, such as realty trusts

Refer to the following regulatory provisions for guidance on the definition of a NOW account:

12 U.S.C. 1832(a), NOW accounts
(This citation is the Act which created NOW accounts.)

Section 329.1(b)(3), footnote 1
(This footnote quotes 12 U.S.C. 1832(a) in its entirety.)

Regulation D, Section 204.2

Regulation D, Section 204.130
(This is an interpretative section providing further guidance on the eligibility of certain entities to maintain NOW accounts.)

Savings Account

Accounts that are subject to the same transaction limitations as MMDAs (including passbook savings accounts and statement savings accounts).

**EXAMINATION
PROCEDURES**

General

Evaluate for Compliance with Part 329

1. Determine which of the following accounts the financial institution offers:

Demand deposits (non-interest bearing checking accounts)
Savings accounts
Negotiable Order of Withdrawal (NOW) accounts
Money Market Deposit Accounts (MMDA)
Time deposits

2. Determine the category of account according to the activity allowed for that particular account.

*NOTE: Even though an account may be classified by the financial institution as one of the above, **the activity allowed within the account** dictates the actual definition. For example, an account which exceeds the monthly transfer or check processing limits should no longer be classified as a savings account but as a MMDA by the institution.*

Refer to Section 204.2 of Regulation D for account definitions.

NOW Accounts

3. Determine whether the entire beneficial ownership interest of a NOW account is held by one of the following eligible individuals or entities:

One or more individuals, including sole proprietorships

A not-for-profit organization operated primarily for religious, philanthropic, charitable, educational, political, or other similar purposes

A government unit of the United States, or any state, county, or municipality of the United States, or any United States territory or possession

A fiduciary (either individual or corporate) if the beneficiary is otherwise eligible to maintain a NOW account

Pension funds, escrow accounts, and security deposits if the entire beneficial interest is held by one of the eligible individuals or entities listed above

**EXAMINATION
PROCEDURES
(cont'd)**

**NOW Accounts
(cont'd)**

If an account holder(s) does not meet the above definitions, it is ineligible to maintain a NOW account. For example, for-profit partnerships and corporations are ineligible.

Refer to Section 204.130 of Regulation D for further guidance.

4. Determine if the financial institution has adequate internal controls to ensure that ineligible entities do not maintain NOW accounts.

Review the NOW account trial balance

Use existing records, but if warranted, request a **full name** listing of the trial balance as opposed to a short name version. A short name listing may not include certain portions of the account title; therefore, some ineligible accounts could be missed during the review.

Select questionable accounts, including but not limited to the examples below, for documentation review

- Accounts which include the designations "Inc.," "Corp.," or "P.C." (Professional Corporation), which imply an incorporated entity
- Accounts which include the designation "partnership," "limited partnership," or "general partnership"
- Accounts which include the designation "d/b/a" ("doing business as")

A sole proprietorship using this designation may hold a NOW account. Additionally, the Federal Reserve has taken the position that a group of individuals, related by blood or marriage, that are operating as a family business which is not incorporated and is not a partnership under state law, may also be considered as eligible to hold a NOW account. Depending on state law, such an entity may use the designation "d/b/a" in its title. However, simply because a business has a "d/b/a" designation, it **is not** automatically qualified to hold a NOW account. Corporations and other for-profit entities can be parties to business arrangements which use the designation "d/b/a," and these **are not** considered to be any form of "sole proprietorship" for the purposes of 12 U.S.C. 1832(a) and the other regulatory provisions cited under the definitions of a NOW account in this Manual.

**EXAMINATION
PROCEDURES
(cont'd)**

**NOW Accounts
(cont'd)**

<p>-- Any other account having a title which appears to be that of a business</p>
<p>5. Request the signature cards and the related tax identification numbers of the accounts selected.</p> <p><i>NOTE: Be aware that a sole proprietorship, corporation, partnership, or other formally organized legal entity is generally required under state law to file and have approved articles or a certificate of incorporation (or organization, depending upon the type of legal entity). Furthermore, a non-profit entity, as designated by the Internal Revenue Service (IRS) will have a certificate attesting to their non-profit status issued by the IRS. Actual IRS documentation is not required. However, the institution may have these items on file, or may be able to obtain them from the account holder to assist in the determination of eligibility status.</i></p>
<p>6. Cite as violations of Section 329.1 accounts held by ineligible entities.</p> <p><i>NOTE: In some instances, financial institutions may contend that the "grandfather clause" in Section 204.130(f) of Regulation D exempts any ineligible NOW accounts opened on or before August 31, 1981 from violating Part 329. However, the FDIC does not support this position.</i></p>
<p>7. To support violations, copy and keep in the workpapers the following, as applicable:</p> <p style="padding-left: 40px;">Signature cards</p> <p style="padding-left: 40px;">Partnership agreements or articles of incorporation/organization</p> <p style="padding-left: 40px;">Any other identifying documentation</p>
<p>8. When violations of Section 329.1 occur, do the following:</p> <p style="padding-left: 40px;">Request management to review all NOW accounts to detect other accounts that may be maintained by ineligible entities</p> <p style="padding-left: 40px;">Have management move any such depositors' funds to other accounts for which they qualify, such as a demand deposit or MMDA</p>

**EXAMINATION
PROCEDURES
(cont'd)**

**Money Market
Deposit Accounts
(MMDAs)**

9. Interview personnel responsible for opening NOW accounts to ensure they know the requirements and prohibitions of Section 329.1

NOTE: Check to see if the opening of accounts in violation of Section 329.1 can be traced to any one individual employee or location.

10. Determine if the financial institution has internal controls in place to monitor excessive MMDA activity. Most institutions monitor MMDA activities through either:

Manual procedures (case by case review)

The report may identify the total number of transactions made during the month, but individual account transactions may not be listed until a certain number (for example, three or six) have occurred, or

An excessive MMDA transaction report

Request a copy of the excessive MMDA transactions report. If such a report is not available, review MMDA periodic statements for a six month period.

NOTE: Review the report to determine whether it identifies the specific type and number of transactions. Some reports, for example, may not list transactions until a certain trigger number is reached (for example, three or six). If the report or the account statements do not readily identify the specific type of transaction or whether excessive account activity has occurred, the examiner may need to review individual transaction records.

*It may be difficult to determine the specific type of transaction from financial institution documentation and, therefore, to determine if excessive account activity has occurred. For example, certain financial institutions may classify ATM withdrawals and debit card purchases in the same manner. ATM withdrawals **are not** considered to be part of the six allowed transfers, while point of sale transactions **are** part of the six allowed transfers. As a result, individual transaction records may have to be reviewed.*

**EXAMINATION
PROCEDURES
(cont'd)**

MMDAs (cont'd)

NOTE: When an ineligible entity is consistently allowed to make more than the permitted number of withdrawals or transfers, the MMDA will be deemed to be a demand deposit account. Accordingly, cite a violation under Section 329.2 for payment of interest on a demand deposit if interest was paid during the statement cycle within which the excessive activity occurred. However, no MMDA will be deemed a demand deposit or cited as a violation merely by virtue of exceeding the six transfer limitation if the depositor is eligible to maintain a NOW account.

Do not cite violations of Regulation D within the Compliance Report of Examination if the financial institution does not have procedures to monitor excessive MMDA activity. Address an absence or weakness of procedures on the Examiner's Comments and Conclusions page, or page A, depending upon the extent of non-compliance with Part 329.

11. For customers who continue to violate the MMDA transfer limits after they have been contacted by the financial institution, the financial institution should either:

Eliminate the transfer and draft capabilities of the account, or

Close the account(s) and place the funds in another account for which the depositor is eligible

12. Ensure that no more than the permitted number of transfers or withdrawals are made. A financial institution should either:

Prevent withdrawals or transfers of funds from the MMDA in excess of the regulatory limits, or

Adopt procedures to monitor transfers on an ex post basis and contact customers who exceed established limits on more than an occasional basis

Refer to footnote 5 of Section 204.2(d)(2) of Regulation D for further guidance on the procedures an institution should follow to ensure that MMDAs are properly maintained.

**EXAMINATION
PROCEDURES
(cont'd)**

MMDAs (cont'd)

13. Violations of Section 329.2, Payment of Interest on Demand Deposit Accounts, could have reserve requirement ramifications. Additionally, accounts not cited as violations which are incorrectly accounted for by the institution (MMDA accounts that should be classified as NOW accounts) also could have reserve requirement ramifications. If examiners determine that reserve requirement ramifications are present, follow the procedures below:

Prepare a memorandum and forward it to the appropriate Division of Supervision (DOS) Regional Director to serve as notification of the issue

Submit a copy of the memorandum to the appropriate DCA Regional Manager with the Compliance Report of Examination

The memorandum should detail the following items:

The nature of the apparent violation(s) of Section 329.2

The possibility of an impact on reserve requirements

NOTE: Regulation D requires financial institutions to maintain different levels of reserves against transaction accounts versus other account types, such as time or savings. If, for example, a financial institution is reporting an account as a savings account, when the activity within the account defines it as a transaction account, the financial institution's reserve requirement may be understated.

**Savings
Accounts**

14. Determine if the institution allows the types of transactions from savings deposits which are subject to the six transfer limitation.

Savings deposits, including passbook savings accounts and statement savings accounts, are subject to the same transaction limitations as MMDA accounts and when excess activity is detected, these accounts become demand deposits. Be aware of:

Commercial demand deposit accounts linked to savings accounts, where overdrafts in the demand account are covered by transfers from the savings accounts in excess of prescribed limits

ACH (automated clearing house) transfers from passbook savings accounts to third parties to pay, for example, recurring insurance premiums

**EXAMINATION
PROCEDURES
(cont'd)**

**Savings
Accounts
(cont'd)**

NOTE: Also, like MMDAs, no savings accounts will be deemed a demand deposit account or cited as a violation of Part 329 if the depositor is eligible to maintain a NOW account.

15. If such transactions are permitted, determine, as noted above for MMDAs, if the institution has developed a system to monitor such transactions, and what action is taken against account holders who exceed the limitation.

**Cash
Management
Services**

16. Determine if the financial institution offers cash management services.
- If so, determine if the financial institution's procedures regarding cash management services prohibit the payment of interest on demand deposit accounts.

**WORKPAPER
STANDARDS**

Standardized workpapers must be completed when reviewing compliance with Part 329. Refer to the Standardized Workpapers Appendix in this Manual.



**FDIC LAW,
REGULATIONS
, & RELATED
ACTS**

Applicable Rules

Regulation D, Volume 3, Page 7571

Part 329, Volume 1, Page 2311

**Advisory
Opinions**

An Electric Cooperative is Eligible to Hold a NOW Account under Revised Federal Reserve Board (FRB) Regulation, Letter #91-79, Volume 1, dated 9/27/91, Page 4590

Business Partnership and NOW Accounts, Letter #87-19, Volume 1, dated 10/19/87, Page 4265

Deposits of Real Estate Trust Accounts ("RETA") Program Established by State Statute May, Like IOLTA Deposits, be Held in NOW Accounts, Letter #91-86, Volume 1, dated 11/18/91, Page 4596

Eligibility of Rural Electric Association Cooperative to Hold Funds in NOW Account, Letter #87-43, Volume 1, dated 12/1/87, Page 4281

FDIC Defers to Federal Reserve Board's Interpretation of NOW Accounts, Letter #91-3, Volume 1, dated 1/15/91, Page 4522

Whether ATM Promotion Constitutes Payment of Interest on Demand Deposits, Letter #91-19, Volume 1, dated 3/13/91, Page 4533

Whether Certain Deposit Product Violates Prohibition Against Paying Interest on Demand Deposits, Letter #92-27, Volume 1, dated 4/25/92, Page 4631

Whether Excess Funds From "Sweep" Accounts May be Transferred to Interest-Bearing Account, Letter #93-82, Volume 1, dated 12/6/9, Page 4824



**FDIC LAW,
REGULATIONS
, & RELATED
ACTS**

**Statements of
Policy**

None

**DCA
MEMORANDA**

Examination Procedures for Part 329 – Interest on Deposits, Transmittal
#DCA-96-010, dated 1/31/96

General Workpaper Standards and Standardized Workpapers, Transmittal
#DCA-96-003, dated 1/19/96

Pre-Examination Planning (PEP) Procedures, Transmittal No. DCA-96-013,
dated 1/31/96

**FINANCIAL
INSTITUTION
LETTERS (FIL)**

None
